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Monthly Letter on
Economic Conditions
Government Finance

New York, April, 1949

General Business Conditions

THE month of March has been another period of caution and uncertainty. Some signs of seasonal improvement have appeared, and many expect the trade and employment figures to look better as Spring advances and outdoor work opens up, but the common attitude is to wait and see. While farm prices have been steadier, industrial prices have been weakening. The most noteworthy development of the month has been the marking down of lead and zinc prices in the primary markets, following a series of declines in scrap metals of all kinds. Special interest attaches to metal markets because they reflect the activity and sentiment of a great variety of industries. When farm prices dropped early in 1948 metals did not follow, and their firmness was pointed to at that time as indicating that the general situation was not much affected. By the same test, their decline now reflects a more widespread weakening of industrial demand.

Further scattered layoffs of factory workers have been reported during the month, and the two-weeks' coal mining shutdown order by Mr. Lewis put both miners and railway employes out of work. Thus unemployment has been larger than in February when, according to the Census Bureau's estimate, it reached 3,200,000. Likewise, the Federal Reserve Board's index of industrial production for March is expected to show a sharper decline than in February, when it dropped two points to 189 (1935-39 = 100). The peak was 195 last October and November.

On the other hand, the rise in the unemployment compensation rolls is levelling off, according to the latest weekly figures. With seasonal influences now favorable, U. S. Department of Labor officials say confidently that little or no further increase in unemployment is to be expected over the next few months, and they add that employment will again reach 60,000,000 at the seasonal peak next Summer. Similarly, April production indexes will be helped by the resumption of mining, while operations in steel, automobile and a good many other industries still having large backlogs are being sustained. Output of passenger automobiles in the second quarter is expected to exceed the first quarter. A seasonal upturn in building contract awards has appeared, with February up from the January low and March showing a further gain.

Retail trade reports are difficult to interpret because Easter this year is three weeks later than last and comparisons are distorted. During March department store sales have been sharply below a year ago, but the later Easter will bring compensating gains in the first half of April.

Buyers Shortening Commitments

Overall figures such as the foregoing suggest that production and consumption, during this period of slackening, have declined less than prices and new orders reaching the industries have declined. Undoubtedly that is the case. The chief influence in the current situation is the caution of buyers and their effort to reduce inventory

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and minimize commitments. This applies both to merchants and to industrial purchasing agents. Inventory fluctuations are always a powerful factor in business swings. During the upswing, accumulation augments current demand. When accumulation ceases, total demand shrinks correspondingly, and if inventory is reduced, demand falls below current consumption. Forward commitments make even wider swings.

Since the end of the war the country has been going through a period of replenishment and additions to inventories. It now seems clear that this accumulation has come to an end, except as shipments still come forward on old orders or as the slackening may cause stocks of finished goods to rise temporarily in some lines. The weakening of demand is accentuated because it weakens prices, and the expectation of still further price declines causes buying to be postponed.

Essentially the same influences affect consumer buying. Although it is an economic truism that there is no limit to human wants, there are nevertheless limits to the desire for specific things at specific times. Consumers also have inventories, and their rate of accumulation affects business in much the same way that business inventories do. The long period of "catching up" has put buyers in a position to wait, to look for bargains, to save or pay off debts as alternatives to spending.

Latest figures of personal income are for January. In that month, according to the calculations of the Department of Commerce, the total was at a seasonally adjusted annual rate of $220.8 billions, still almost at the all-time peak of $221.0 billions reached in December. But estimated consumers' purchases of goods and services, seasonally adjusted annual rate, declined $5.8 billions below December, and the rate of consumers' savings increased $5.6 billions. These calculations involve a high degree of estimation, but taking them as they stand they provide, together with the shortening of business commitments, a persuasive explanation of the change in the business situation.

Another influence on buying is the fact that prices of things wanted by many people have risen beyond the means of many. Housing is one, but by no means the only, example. Where this is the case demand will be lifted only by getting prices down. Retailers agree that buyers respond to bargain offerings and that well-made goods at reasonable prices move rapidly into consumption. The problem of the industries is to fit their products to both the wants and the purse of the buyer. The trend is in that direction also. Prices of manufactured goods have been more widely reduced during the past month than at any time since the inflation started. Many home appliances have been marked down, and declines in furnishings, apparel and fuel are contributing, along with cheaper food, to a lower cost of living. Ways are being found to cut costs, and products are being redesigned to bring them within reach of lower-bracket incomes.

Nature of the Adjustments

Everything that can be done to cut costs by increasing productivity, designing goods so they can be made more cheaply, and eliminating waste, contributes toward broadening markets and sustaining demand. Such adjustments will go forward more rapidly under competitive conditions, and with materials and labor more abundant. To be sure, the return to competition cannot be made without effect on the economic situation. The drop in demand and prices puts pressure on high-cost producers. Whenever one drops out someone loses, and stocks of goods or property, or both, have to be liquidated. A shock, however tiny, is imparted to the economic organization. What will count in the long run, however, is the fact that the price adjustments taking place are improving basic economic relationships. They are giving a little relief to whole groups of people who have been the victims of inflation and have lost purchasing power. This is an offset to the loss of income by producers whose markets are shrinking, and by their workers.

It may be added that where lower prices can be achieved through increased productivity, the producer experiences no loss of income, and everyone gains. Conversely, the one thing that would be most harmful in the present situation would be an increase in costs.

Through price adjustments, absorption of stocks and running down of commitments, a new balance is being gradually worked out. In cotton goods the adjustment has been running more than a year. In steel it has barely begun. Other industries fall in between. It is significant, however, that the curtailment is staggered and piecemeal rather than concentrated, for some parts of the economy may be coming up while others are going down. Many retailers already have smaller inventories than a year ago and have gone as far as practicable in hand-to-mouth buying; manufacturers are of the opinion that some stores, particularly in apparel lines, have gone too far, and that they are losing sales because they are not carrying sufficiently varied stocks. The business

downturn will not be deepened and prolonged by drastic liquidation from that quarter, where caution already is extreme.

The strong point in the outlook is that the familiar causes which in the past have produced spiraling or liquidating recessions do not appear to exert heavy weight at the present time. Although business expenditures on plant and equipment are receding moderately from the peak, an enormous amount of work is in progress and going ahead. There is little evidence that cancellations have reached impressive proportions. Public expenditures on construction are large and increasing.

Money is neither dear nor tight, as it has been before nearly all major business declines. Banks generally are liquid and able to take on new loans if good borrowers come forward. If this were not the case, the Federal Reserve authorities could quickly relieve any strain in the supply of credit by rescinding some of last year's increase in reserve requirements. That their policies face in that direction is shown by their action in easing installment selling terms and stock market margin requirements.

Corporate Earnings in 1948

Annual reports now available from a large majority of all American corporations which issue public reports show that while business as a whole established new high records in sales and earnings last year, many branches of industry were down substantially from 1947 because of the effects of increased competition upon volume and upon profit margins. Our tabulation of the published statements of 3,262 corporations in all lines of business shows a combined net income after taxes of approximately $11.7 billion, compared with $9.5 billion in 1947, an increase of 22 per cent. Despite this increase in the total, lower earnings were shown by 37 per cent of all reporting companies.

Most of the increase in net income last year was due to the great expansion in dollar volume of sales, rather than widening of profit margins. Sales or gross income figures given by more than four-fifths of all reporting companies, excluding the finance groups, totaled in excess of $141 billion in 1948, upon which the average margin was 7.3 cents per sales dollar, compared with 6.8 cents in 1947. Of the 65 major industrial classifications used in our tabulation, the average margin was wider in 29 groups, narrower in 33, and unchanged in 3.

While we continue to present the return on net assets as shown by published reports, it should be reiterated that the net amounts at which assets are carried on the balance sheets for accounting purposes are in most cases far below present-day values, owing to the lower costs at which much of the plant and equipment was acquired, to the writing down of assets through depreciation reserves and special charges, and to the sharp increase since prewar in replacement costs. For this reason, the earnings as reported in current dollars greatly overstate the real rate of return being earned.

Mixed Trends in Manufacturing

Of the 1,680 companies in the manufacturing industries, which comprise approximately one-half of the net assets of all reporting companies, the combined net income in 1948 was 23 per cent higher than in 1947. Striking evidence of the changing trend of earnings is shown by the fact that 42 per cent, or nearly half, of the companies had lower net income, including 6 per cent with net deficits. Manufacturers' sales increased by 18 per cent, while the average profit margin widened from 7.1 to 7.5 cents per sales dollar.

As shown by the table, the large increases in net income in the manufacturing industries were confined to a relatively few lines – particularly petroleum, steel, and automobiles, which made heavy investments of additional capital for enlarging plant capacity, and had a tremendous expansion in volume of sales to meet the unprecedented demands for their products. Excluding these three groups, earnings of the remaining 1,555 manufacturers increased 11 per cent.

In the consumers' goods industries generally, the supply last year substantially caught up with demand, resulting in increased competition and the need for price cuts or greater selling expense in order to maintain the volume of sales. In most of these groups, the 1948 earnings were lower than in 1947, measured both by return on net assets and by profit margin on sales.

In lines other than manufacturing, there were increases in net income of most of the group totals last year, despite the substantial number of individual companies having decreases. Both net assets and sales also increased, and the changes in rates of return and profit margins were in most cases relatively small.

Effects of Sales Declines on Earnings

Data given in these columns last month showing how 185 manufacturing companies that experienced sales declines last year fared as to earnings have been revised to include 335 reports in this category now available. Although com-

NET INCOME OF LEADING CORPORATIONS FOR THE YEARS 1947 AND 1948

(In Thousands of Dollars)

No. of Cos.	Industrial Groups	Reported Net Income After Taxes 1947	Reported Net Income After Taxes 1948	Per Cent Change†	Book Net Assets Jan. 1 -a 1947	Book Net Assets Jan. 1 -a 1948	% Return on Net Assets -a 1947	% Return on Net Assets -a 1948	% Margin on Sales -b 1947	% Margin on Sales -b 1948
24	Baking	$ 61,340	$ 68,851	+12.2	$ 301,892	$ 322,314	20.4	21.4	5.0	5.2
17	Dairy products	63,574	64,263	+ 1.1	419,107	460,097	15.2	14.0	2.5	2.4
21	Meat packing	96,032	51,791	—46.1	697,726	721,601	13.8	7.2	1.4	0.7
23	Sugar	78,674	55,903	—28.9	411,092	457,124	19.1	12.2	7.7	6.0
75	Other food products	269,804	246,514	— 8.6	1,270,819	1,419,387	21.2	17.4	5.8	4.6
17	Soft drinks	50,713	49,331	— 2.7	224,499	241,977	22.6	20.4	13.0	11.2
31	Brewing	48,179	48,651	+ 1.0	182,469	213,218	26.4	22.8	9.5	8.0
11	Distilling	138,689	154,251	+11.2	518,769	608,401	26.7	25.4	6.5	7.2
23	Tobacco products	117,484	143,449	+22.1	913,866	1,003,974	12.9	14.3	4.5	5.2
40	Cotton goods	154,709	170,130	+10.0	444,939	540,883	34.8	31.5	11.7	12.2
17	Silk and rayon	85,980	115,861	+34.8	331,471	386,473	25.9	30.0	12.4	13.8
7	Woolen goods	27,482	31,170	+13.4	135,874	148,800	20.2	20.9	7.5	7.1
18	Hosiery, knitted goods	20,316	22,702	+11.7	88,384	102,022	23.0	22.3	9.1	9.2
46	Other textile products	143,418	163,793	+14.2	568,324	663,576	25.2	24.7	9.1	8.7
33	Clothing and apparel	28,432	25,846	— 9.1	157,017	186,901	18.1	13.8	5.5	4.5
9	Leather tanning	10,824	7,314	—32.4	49,320	53,930	21.9	13.6	6.1	3.9
25	Shoes, leather products	38,949	37,203	— 4.5	237,432	253,732	16.4	14.7	4.5	4.1
25	Tires, rubber products	121,087	112,207	— 7.3	758,893	803,207	16.0	14.0	4.4	4.1
29	Lumber	69,120	78,362	+13.4	209,070	267,306	33.1	29.3	11.7	11.2
17	Furniture, wood products	20,876	24,621	+17.9	122,352	137,182	17.1	17.9	6.5	6.6
85	Pulp and paper products	294,208	299,832	+ 1.9	1,242,052	1,469,009	23.7	20.4	11.4	10.6
31	Printing and publishing	45,591	43,642	— 4.3	229,204	250,103	19.9	17.4	6.9	6.2
65	Chemical products	416,110	496,564	+19.3	2,420,796	2,798,643	17.2	17.7	9.6	9.9
29	Drugs, soap, cosmetics	128,678	130,099	+ 1.1	620,191	683,918	20.7	19.0	7.9	7.1
17	Paint and varnish	54,856	46,063	—16.0	288,241	325,257	19.0	14.2	6.0	4.4
44	Petroleum products	1,254,933	1,954,277	+55.7	7,997,753	8,844,742	15.7	22.1	11.1	12.9
28	Cement	26,098	39,712	+52.2	226,306	239,364	11.5	16.6	11.5	14.0
12	Glass products	68,091	68,186	+ 0.1	387,165	426,046	17.6	16.0	8.2	7.8
40	Other stone, clay products	92,916	116,017	+24.9	520,956	613,412	17.8	18.9	9.5	10.0
53	Iron and steel	430,507	566,135	+31.5	3,794,897	4,034,081	11.3	14.0	6.2	6.7
11	Agricultural implements	94,862	136,868	+44.3	860,890	921,946	11.0	14.8	5.9	6.2
77	Building, heat., plumb. equip.	127,893	156,344	+22.2	651,939	745,436	19.6	21.0	7.5	7.9
79	Electrical equip. and radio	283,641	334,621	+18.0	1,423,722	1,632,513	19.9	20.5	5.9	6.0
46	Hardware and tools	53,846	54,330	+ 0.9	284,556	317,454	18.9	17.1	8.7	8.0
43	Household appliances	83,309	87,436	+ 5.0	251,257	314,329	33.2	27.8	8.3	7.6
156	Machinery	182,606	228,868	+25.3	1,076,360	1,184,327	17.0	19.3	7.5	8.0
25	Office equipment	94,383	104,539	+10.8	353,239	408,715	26.7	25.6	10.3	10.5
34	Nonferrous metals	313,422	334,236	+ 6.6	2,120,877	2,236,766	14.8	14.9	12.4	11.7
94	Other metal products	149,326	186,378	+24.8	952,869	1,053,321	15.7	17.7	6.5	6.8
28	Autos and trucks	447,566	632,777	+41.4	2,167,241	2,435,302	20.7	26.0	6.4	7.4
66	Automobile parts	153,941	179,190	+16.4	658,951	761,194	23.4	23.5	7.1	7.1
25	Railway equipment	61,789	65,516	+ 6.0	598,409	643,017	10.3	10.2	6.1	5.4
25	Aircraft and parts	— 35,280	17,571	+ —	587,385	565,047	—6.0	3.1	—4.0	1.4
6	Shipbuilding	4,868	10,483	+ —	84,519	89,220	5.8	11.7	3.2	5.1
53	Misc. manufacturing	93,105	101,377	+ 8.9	541,429	622,102	17.2	16.3	8.5	8.9
1,680	Total manufacturing	6,566,947	8,063,274	+22.8	38,384,019	42,607,369	17.1	18.9	7.1	7.5
33	Coal mining —c	66,191	91,685	+38.5	582,247	617,786	11.4	14.8	6.7	7.9
26	Metal mining —c	45,775	48,346	+ 5.6	353,229	399,414	13.0	12.1	12.7	11.6
44	Oil and gas —c	82,249	143,751	+74.8	341,250	400,051	24.1	35.9	28.9	33.1
12	Other mining, quarrying —c	30,464	34,613	+13.6	125,546	134,034	24.3	25.8	26.4	26.6
115	Total mining, quarrying	224,679	318,395	+41.7	1,402,272	1,551,285	16.0	20.5	13.1	14.5
20	Chain stores — food	50,818	52,619	+ 3.5	284,834	319,288	17.8	16.5	1.4	1.3
61	Chain stores — other	204,705	226,852	+10.8	1,092,387	1,187,436	18.7	19.1	5.0	5.1
43	Department stores	114,131	124,323	+ 8.9	799,405	884,506	14.3	14.1	3.5	3.5
7	Mail order	170,774	201,489	+18.0	787,508	893,270	21.7	22.6	5.0	5.4
62	Wholesale and misc.	93,624	87,344	— 6.7	475,516	540,991	19.7	16.1	3.5	3.3
193	Total trade	634,052	692,627	+ 9.2	3,439,650	3,825,491	18.4	18.1	3.7	3.8
131	Class 1 railroads —d	478,875	711,000	+48.5	12,715,977	13,094,224	3.8	5.4	5.5	7.4
33	Traction and bus	22,102	21,630	— 2.1	456,334	454,970	4.8	4.8	4.5	4.2
12	Shipping	31,268	17,145	—45.2	209,275	226,264	14.9	7.6	8.7	3.1
16	Air transport	— 11,693	— 403	—	237,897	240,123	— 4.9	— 0.2	—3.0	—0.3
51	Misc. transportation	24,417	23,068	— 3.1	253,606	255,801	9.6	9.3	8.7	8.1
243	Total transportation	544,969	773,040	+41.9	13,873,089	14,271,382	3.9	5.4	5.3	6.9
196	Electric power, gas, etc —d	617,236	638,559	+ 3.5	6,794,915	7,122,475	9.1	9.0	14.7	13.5
66	Telephone and telegraph —d	185,934	244,941	+31.7	3,208,309	3,348,021	5.8	7.3	7.2	8.2
262	Total public utilities	803,170	883,500	+10.0	10,003,224	10,470,496	8.0	8.4	11.9	11.4
14	Amusements	58,330	28,309	—51.5	440,242	462,029	13.2	6.1	7.9	3.9
45	Restaurant and hotel	16,033	14,385	—10.3	127,217	130,236	12.6	11.0	5.3	4.6
30	Other business services	28,063	29,691	+ 5.8	162,555	179,433	17.3	16.5	7.6	7.1
19	Construction	14,313	19,064	+33.2	91,509	100,057	15.6	19.1	4.0	3.7
108	Total amusements, services, etc.	116,739	91,449	—21.7	821,523	871,755	14.2	10.5	6.7	4.7
287	Commercial banks —e	396,391	441,950	+11.5	5,067,171	5,286,664	7.8	8.4	—	—
72	Fire and casualty insurance —e	35,339	130,966	+ —	1,444,522	1,446,563	2.4	9.1	—	—
146	Investment companies —e	147,346	176,348	+19.7	2,445,613	2,534,064	6.0	7.0	—	—
63	Sales finance companies	57,030	90,166	+58.1	539,008	585,536	10.6	15.4	—	—
93	Real estate companies	11,051	12,357	+11.8	109,716	116,859	10.1	10.6	—	—
661	Total finance	647,157	851,787	+31.6	9,606,030	9,969,686	6.7	8.5	—	—
3,262	Grand total	$9,537,718	$11,674,072	+22.4	$77,529,807	$83,567,464	12.8	14.0	6.8	7.3

a—Net assets at the beginning of each year are based upon the excess of total balance sheet assets over liabilities; the amounts at which assets are carried on the books are far below present-day values. b—Profit margins computed for all companies publishing sales or gross income figures, which represent over four-fifths of total number of reporting companies, excluding the finance groups; includes income from investments and other sources as well as from sales. c—Net income is reported before depletion charges in some cases. d—Due to the large proportion of capital investment in the form of funded debt, rate of return on total property investment would be lower than that shown on net assets only. e—Figures represent in most cases operating earnings only, and do not include gains or losses on investments. † Increases or decreases of over 100% not computed. — Deficit.

panies with decreased sales comprised only about one out of every five last year, their number may be expected to increase as the upward curves of business activity and prices flatten out or decline.

For this group showing sales decreases, the 1948 sales amounted to $9.7 billion and the net income to $451 million, while the average decline in sales was 14 per cent, but in net income 47 per cent. A comparison of the figures according to size of the sales decrease is given below:

Average Percentage Change, 1947-48, in Sales and Net Income of 335 Manufacturing Corporations Reporting Sales Decrease

Sales Decrease	Number of Companies	Average Change: Sales	Average Change: Net Income
1 to 10%	166	— 5%	—24%
11 to 20%	89	—15%	—46%
21 to 30%	53	—25%	—75%
Over 30%	27	—42%	—Def.
Total	335	—14%	—47%

Although these average changes form a fairly regular pattern, the changes in industry groups and among individual companies were extremely uneven. For example, 51 of the companies having sales decreases were nevertheless able to show an increase in net income – owing to control over expenses or, in some instances, to special circumstances, such as unusually heavy charges incurred in 1947. At the other extreme were 39 companies which swung from profits in 1947 to deficits in 1948.

The accompanying table shows the breakdown of the figures for those industrial subgroups in which there were five or more companies reporting sales decreases.

Average Percentage Change, 1947-48, in Sales and Net Income of 335 Manufacturing Corporations Reporting Sales Decreases

No. of Cos.	Industrial Groups	1948 Totals (000s) Sales	1948 Totals (000s) Net Income	Aver. % Change Sales	Aver. % Change Net Income
5	Baking	$ 57,870	$ 1,355	—12	—61
15	Sugar	660,630	37,452	—15	—42
22	Other food products	2,039,910	80,823	—10	—48
6	Soft drinks	57,585	4,238	— 3	—84
16	Brewing and distil.	1,145,521	75,882	—13	—60
7	Cotton goods	245,479	35,246	—10	—25
6	Other textile prod.	150,479	9,802	—11	—30
7	Clothing & apparel	100,359	2,104	— 3	—19
14	Leather and shoes	190,275	4,608	—16	—63
13	Tires, rubber prod.	956,945	40,295	—14	—48
18	Pulp & paper prod.	248,078	24,031	—12	—52
9	Drugs, soap, cosmet.	333,217	13,807	—12	—39
16	Building equip.	160,261	12,578	—11	—27
14	Elec. equip. & radio	159,216	7,145	—24	—63
10	Hardware and tools	84,523	5,236	—15	—41
10	Household appliances	228,942	15,669	—23	—79
41	Machinery	457,829	26,978	—17	—29
36	Other metal prod.	1,006,562	33,258	—14	—53
9	Autos and trucks	348,766	8,199	—20	—74
11	Automobile parts	169,176	11,872	—13	—27
50	Other manuf.	861,717	50,964	—11	—48
335	Total	$9,663,340	$450,542	—14	—47

The percentage declines in sales and net income are computed as simple averages of all reports included and are not weighted as to the relative size of the different companies, whose sales ranged from under $1 million to over $1 billion. While these figures illustrate the general pattern, the available sample is of course too small either for measuring the trends accurately, or for determining "break-even points". The principal fact brought out is the difficulty, when the total volume of business falls off, of bringing about a corresponding reduction in the total of expenses, many of which are not only high but relatively rigid.

In a period of lessened inflationary pressures, with lower raw material prices and possible increases in labor productivity, adjustment of expenses to decreased sales may prove less difficult for many companies than during the generally rising trend of costs in 1948.

The Argument About Profits

The figures on corporate earnings for 1948, now appearing in the press and summarized in the preceding article, will no doubt generate fresh controversy on the subject. Reports of record-breaking earnings may encourage proposals for distributing these "excess" earnings by taxes, wage increases, or government-dictated price reductions to consumers.

Such agitation against profits is both ill-founded and dangerous. Profits in a freely competitive market are largely the product of the impersonal workings of economic law. When the demand for goods exceeds the supply, as has been the case most of the time since the war, prices and profits naturally rise. Individual concerns may try to buck the trend by lowering prices, as did International Harvester and Ford two years ago, to cite two conspicuous examples. Such efforts are praiseworthy but unavailing under inflationary conditions. The concerns soon find that, with rising wages and other costs, they are only penalizing themselves without making any significant dent in a market characterized by the insistent pressure of too many dollars chasing too few goods.

Many of our largest corporations, which have been subjected to the most severe criticism, held their prices well below what the traffic would bear, as measured by prices in "gray" and second hand markets for steel sheets and pipe, automobiles and trucks, farm implements, electrical equipment, textiles, and numerous other articles. But buyers who wanted the goods and were willing to pay premiums to get them bid up the prices, and the profits, instead of going to the original sellers, went to intermediate processors and distributors.

Not even government, with all its authority and paraphernalia of controls, has been able to suppress completely this law of supply and demand. Save where controls have had broad public support, as in time of war, trading has to a large extent been driven underground, and black marketeers have reaped a harvest at the expense of legitimate business. The public – if it wanted the goods – had to pay the true rather than the controlled price.

In short, as stated before in this Letter as long ago as December 1919 –

> In time of real scarcity prices are bound to go up, for there is an economic necessity for it, and somebody is sure to make money out of the rise. The only remedy for high prices and abnormal profits is increased production – greater supplies on the market. The evil will work its own cure if let alone, and all efforts to mitigate its effects are likely to interfere with the natural restoration of normal conditions. We do not say that price regulation is never advisable or justified. Circumstances may be such that immediate relief is of the first importance, and the natural laws require time to do their work, but in the long run they do their work effectively.

The danger in attempts to place arbitrary limits upon profits is that, over the long run, they will diminish the principal incentive and source of capital for improving the industries and raising the standard of living. They may kill the goose that lays the golden eggs.

"Real" and "Unreal" Profits

Much has been said about "real" and "unreal" profits, and the distinction is warranted in view of (a) the large element in profits of nonrecurrent inventory gains, which were absorbed in inventory replenishment at higher prices, and (b) the inadequacy of depreciation charges based on the low original costs of plant and equipment.

The Department of Commerce, in its much quoted estimates of total corporate income, has figured the inventory factor alone in corporate profits at approximately $5 billion in both 1946 and 1947, and over $3 billion in 1948. Including under-depreciation, Professor Sumner Slichter, of Harvard University, estimated in testimony to Congress that during the past three years American corporations "overstated" their earnings by about $16.4 billion. This, he said, is the amount by which the reported statements of profits exaggerate the income available to pay dividends, to expand plant, to increase wages, or to reduce prices.

The Purchasing Power Theory

Now that the business boom seems to be receding, we may hear more of the theory that business depressions are brought on by lack of consumer purchasing power caused by too much of the national income flowing to profits and not enough to wages and other segments of the national income.

The report of the Congressional Joint Committee on the Economic Report (Chairman, Senator O'Mahoney), rendered in February, reflects this viewpoint:

> If one compares 1939 and 1948 one finds that payrolls before taxes fell behind from 61.9 to 59.9 per cent of the total national income, the corresponding share of corporate profits increasing by more than one-half from 10.0 per cent to 15.6 per cent.
>
> Corporate profits after taxes of $5.005 billion in 1939 amounted to 7.7 per cent of the national income originating in the private sector of the economy ($64.3 billion; i.e., national income, $72.532 billion minus compensation of government employees, $8.2 billion). In 1948 that percentage had increased to 9.5 per cent, a figure dangerously close to the excessive ratio of 10.1 per cent in 1929. As need hardly be mentioned, 1929 was a year of such abnormality of economic relationships that it was followed by one of the worst depressions in economic history.

Dr. Leon Keyserling, vice chairman of the President's Council of Economic Advisers, in an article in the New York Times Magazine of January 9, said:

> To achieve a workable balance between production and consumption in a more normal peacetime economy, consumer expenditures will need to assume a relatively larger role. And the preliminary indications are that the changing structure of national income does not bode well for this orderly transition. Compensation of employes has dropped from 65.9 per cent of the national income total in 1939 to 61.6 per cent in the fourth-quarter of 1948, while corporate profits and inventory valuation adjustments have risen from 8 per cent to 14.7 per cent.

Harping on the same theme is "Economic Outlook", monthly publication of the CIO. Referring to the "dangerous trend shown by the declining share of the national income of all wage and salary earners," it says in the January issue:

> While compensation of employes took 67½ per cent of the total in 1945, it had been chopped to 61 per cent by 1948. In the same period profits before taxes increased from 11 per cent to 15 per cent of the total income.

A Look at the Figures

Looking at the figures, the first comment that can be made relates to the selection of the data for comparisons. As we have pointed out before, in dealing with such constantly fluctuating variables as national income and its components, almost anything can be shown depending on what years you take.

For example, the Committee on the Economic Report, cited above, refers to the profit component of national income in 1948 as being "dangerously" close to the "excessive" ratio in 1929, and goes on to suggest darkly that 1929 was a

year of such "abnormality" of economic relationships that it was followed by one of the worst depressions in history.

What the Committee did not point out is that the total employe compensation at 62.1 per cent of national income in 1948 was actually *greater* than the 58.1 per cent in 1929, while the share of private wages and salaries (excluding government) at 51.5 per cent in 1948 was practically the same. The groups that have lost ground, relatively, as compared with 1929 do not include the wage and salary earners, nor the farmers whose proportionate share of the national income increased from 6.5 to 8.5 per cent. They include landlords whose cut of the national income "pie" shrank from 6.6 to 3.5 per cent, corporate stockholders whose dividend share was cut in half from 6.6 to 3.3 per cent, and investors in fixed income obligations whose interest share shrank by more than two-thirds, from 7.4 to 2.2 per cent.

The decline between 1939 and 1948 in the proportionate share of national income going to wages and salaries, along with an accompanying rise in the share going to profits – which bothers the Committee on the Economic Report and Dr. Keyserling – would appear to be a natural manifestation of the tendency, as business expands towards capacity, for profits to rise more rapidly than wage payments. And 1948 was a year of boom against a good deal of slack in the economy in 1939.

Profits Also "Purchasing Power"

To imply that such a shift in the income pattern would cause a depression is to assume a great deal, and certainly oversimplifies a highly complex problem. It must not be overlooked that income in the form of profits constitutes "purchasing power" just as much as income in the form of wages. It is, indeed, an extremely dynamic form of purchasing power, for, as the record of business cycles shows, it is the fluctuations in business expenditures for inventories, for plant and equipment, etc., rather than fluctuations in consumer expenditures, that make the great difference between booms and depressions.

The foregoing is not, of course, to contend that consumer purchasing power is not significant, and that there is no such thing as important groups of consumers being priced out of the market, with deleterious effects on the whole economy. If large numbers of people either can't buy because prices are too high, or won't buy because they think they are too high, business inventories accumulate and the whole business process begins to back up all along the line.

Who Is Pricing Whom Out of the Market?

But the real question is, who is being priced out of the market, and by whom? Strongly organized wage earners may be able to achieve sufficient wage gains for themselves to enable them "to buy back the product", but what of the effect of such wage increases, translated into higher prices, upon the purchasing power of other groups of the population whose incomes have lagged – landlords, corporate shareholders, and recipients of income from interest, pensions, etc.? What of the effect of increases in farm income, reflected in higher food prices, on the purchasing power of these groups, and upon the purchasing power of labor as well? While it is true that profits, also, are a factor in prices, the fact that total wages and salaries (including unincorporated business and government) exceeded corporate net incomes last year in the ratio of over 6 to 1, and exceeded corporate dividends by over 17 to 1, indicates the relative importance of these elements in general prices and the cost of living.

For this whole complex of questions involved in the as yet far from fully explored problem of what makes business cycles, the CIO seems to have but one answer – propounded repeatedly, and reiterated last month in that organization's weekly newspaper, the CIO News. "Substantial wage increases will provide a great reservoir of buying power." Corporation profit "must be trimmed for the common good."

A Dangerous Prescription

With consumers already rebelling against high prices, and with the profit margins of business diminishing and in many cases disappearing, can the consequences of dosing the economy with such medicine as prescribed above be other than as set forth by Dr. L. Albert Hahn, in his book, "The Economics of Illusion", published in February of this year? –

> If at this juncture the general wage level is pushed upward in accordance with the purchasing power theoretical approach, there is no doubt about what will happen. The wage earners who remain employed will of course have more to spend if their wages are raised. However, the aggregate purchasing power of the economy cannot be pushed up through raising wages by political action. Wages will act as cost factors, no matter what is done. The further rise of the already very high break-even points in many industries will bring about a contraction because more and more enterprises will be forced out of business, and unemployment will ensue.
>
> If we are really heading for deflation, not inflation – which was the government theory only a short time ago – demand must be supported by radical tax relief measures

and ultimately by public works. Both would enhance the aggregate purchasing power of the economy without raising costs. But the raising of wage rates — as against aggregate wages by employing more people — will always be the worst method of increasing purchasing power; for there is no way of evading the fact that wages are the most important cost factor of enterprise. Should a policy of wage-raising really be pursued and the purchasing power theory get the upper hand once more, the recession we may be facing would have a good chance of developing into a serious and protracted depression.

Who Are They?

Testifying before the Senate Banking and Currency Committee on February 3, Raymond M. Foley, Federal Housing and Home Finance Administrator, stated that 29.8 per cent of American non-farm families have incomes of less than $2,000 a year, and 4.6 per cent have incomes of less than $500 a year. These figures, according to press despatches, surprised the Committee, and Senator Ralph E. Flanders of Vermont was led to interject: "Incomes as low as that are just incredible to me. I want to know more about these people and their earnings. I want to know who they are and where they are."

The question was and is important, not only in conjunction with the plans Mr. Foley was supporting — to subsidize rents, tear down slums, and encourage cheaper housing — but also and more generally in conjunction with far-reaching Administration proposals to extend the old-age pension system, increase unemployment benefits, add medical insurance and disability features, enlarge relief contributions, and so on — all in the good name of "welfare" and all to be financed by additional taxes to be levied on business and the working population.

Few people question the desirability of "welfare." Neither can anyone properly forget that it is work and production, after all, that determines how much "welfare" there is to distribute among the citizens.

Senator Flanders' question was left unanswered at the hearings and he urged that some intensive study be undertaken, parallel to action on housing, to help persons in the lowest brackets to increase their earnings. It was indicated that another Senate Committee might take on this task. Meanwhile, by reference to readily available sources, it is possible to formulate at least some of the answers, as well as problems and difficulties, a study of this kind is likely to produce.

Data Based on a Poll

The figures Mr. Foley presented at the February 3 hearings, as reported in the press, differ from another set he gave on February 11 at hearings of the Joint Congressional Committee on the Economic Report. Meanwhile, the Bureau of the Census, from which Mr. Foley evidently drew his figures, released under date of February 7 a pamphlet on "Income of Families and Persons in the United States: 1947." This pamphlet carries twenty-odd tables of income distribution data arranged in a variety of ways.

These 1947 data were prepared by the Census Bureau on the basis of a poll of 12,000 "households." In drawing on the data it must be borne in mind that the margins of error in the polling technique, inevitable to the method, are widened when the question of income enters in. People are naturally sensitive about their incomes and any tendency to exaggerate is apt to evaporate when the questioner comes as a representative of Government which has the taxing power and dispenses relief. Moreover, people tend to regard "take-home pay", after numerous deductions, as their total money incomes. Persons with irregular incomes are under no compulsion to keep a record of income unless the aggregate runs above their income tax exemption limits. The Census Bureau, indeed, specifically warns against "reporting biases" which produce understatements of income and explains:

> In most cases the schedule entries for income are based on memory rather than on records, and in the majority of instances on the memory or knowledge of some one person, usually the wife of the family head. The memory factor in data derived from field surveys of income probably produces underestimates, because the tendency is to forget minor or irregular sources of income. Other errors of reporting are due to misrepresentation or to misunderstanding as to the scope of the income concept.

If incomes are understated, it is plain that the numbers of people shown with incomes below $500, or below any other limit, is *overstated.* Unfortunately, no one can tell how much this may amount to.

With this essential qualification in mind, what does the poll show? The Census Bureau's income distributions are uniformly presented in terms of percentages of individuals or families. But the report also gives the numbers to which the percentages apply and this makes it possible to convert the figures into the more meaningful terms of estimated numbers of persons or families involved.

The "Not Employed" with Small Incomes

Since "family income" is made up of the incomes of family members, essential insight is afforded by the Census figures on the distribution of incomes among individuals. Of the 107,000,000 *persons* 14 years of age and over, nearly three-

fourths are shown with incomes of less than $2,000, and almost half – fifty million – with incomes of less than $500. These proportions, incredible on the face of it, are rather simply explained. Most of the fifty million people with incomes of less than $500 were "non-working" housewives and students. The Census figures do not show how many, but it is significant that, of the 50,000,000, there are 41,000,000 listed as "Not employed or in the armed forces in April, 1948."

The official government estimate of unemployment (that is, of employable persons seeking work) in April, 1948 was 2,193,000 and many of these persons could have had incomes well above $500 during 1947, even if they were unemployed for some time during that year. Since $500 is below the minimum pay scale in the armed forces, the conclusion is forced that very few of the 41,000,000 "Not employed or in the armed forces" with incomes under $500 were "employable" and looking for work in 1947. Besides the obviously large content of housewives and students, who were they? There are two minor but significant groups concealed in the total: (1) "unemployables"; (2) people living on past savings.

The "unemployables" include those physically unfit as well as those congenitally disinclined to work. The livelihood in either case may be provided by relatives, by private charities, or by state or local governments sometimes supplemented by funds from the Federal Treasury.

People living on past savings run of course through all income brackets. In the under-$500 group is always hidden a concentration of retired persons who are dipping into their principal funds (including insurance proceeds and bequests) to supplement small returns from dividends, interest, rents, and pensions. In this group are also uncounted numbers of active people taking a respite from their normal work or between jobs. While not the *same* people from year to year, there are always some in *every* year.

It is of incidental interest that the Census figures also show 100,000 "not employed" persons with incomes of $6,000 and over. This affords a crude idea of the possible dimensions of the class of so-called "idle rich", although a $6,000 income – within easy reach of a skilled artisan in many trades today – is not one that most people think of as representing capacity to enjoy untold luxury. These are people who are always approached when funds are needed for worthy causes. They are also called upon to turn over more than one-quarter, and often more than one-half, of their taxable incomes above $6,000 to the Bureau of Internal Revenue.

The Employed with Small Incomes

Of the fifty million persons with incomes under $500, nine million is indicated as the total of "employed" persons with incomes of under $500. This is nearly one out of six in the civilian labor force. How can this be, in light of what everyone knows about prevailing wage and salary scales, unemployment benefits, and the minimum $16 a week under the Federal Wage and Hour Law?

That there is a "joker" here is evident when one finds that the Census Bureau has 4, 000,000 persons "employed" but without any income at all. This curiosity is explained by a miscellany of circumstances. Some, supported by others, give their services free, as in charitable activities. One large element is the boy or girl (14 years of age or over) helping out on the farm or in the family business without a money consideration. Another actor is the unincorporated business man, farmer, or investor who suffered losses in 1947 – as some hundreds of thousands do in years of even the most general prosperity. Again, there is the doctor, lawyer, or dentist just starting out in practice whose business expenses may equal or exceed his income. One large part of the 4,000,000 employed who had no income evidently is explained by the technicality that the Census figures for income were for 1947 while employment status was that of April 1948. In other words, many of the people recorded as employed were not actually working in 1947.

When a few dollars of income, from some source or other, are added to such "no income" llustrations, we account for many of the 5,000,000 "employed" persons shown in the $1 to $499 income range. Also in this grouping would be retired persons who accepted some odd jobs, and students working after school.

The Unattached Individual

In its report the Census Bureau also gives figures for combined incomes of families, and incomes of individuals not in families. As the first column in the following table indicates, two and a half million – nearly one out of three – of the individuals not in families show an income of less than $500. Many in this group, while living away from home, receive some support from home, or have resources in the shape of bequests, life insurance proceeds, savings from earlier working years, and so on. Some are students, aspiring actors and artists, beginners in business or the professions. Others are widows or widowers supplementing small incomes by drawing on savings, help from children, and so on. Finally,

of course, are those who are public charges, vagrants, refugees from the complex society.

Family Statistics

The second, third, and fourth columns of the table deal with the pooled income of "families", a "family" being defined as two or more relatives living together. Shown separately are families resident in centers of more than 2,500 population ("urban"), in smaller centers but not on farms ("rural-nonfarm"), and on farms ("rural-farm").

Distribution of Income Among Persons and Families in 1947
Based on Poll Taken by the Bureau of the Census

Money Income Range	Individuals not in families	Families: Urban	Families: Rural non-farm	Families: Rural farm
Under $500	2,560,000	490,000	370,000	760,000
$500 — $999	1,520,000	940,000	550,000	870,000
$1,000 — $1,999	1,890,000	2,990,000	1,510,000	1,680,000
$2,000 — $2,999	1,230,000	4,960,000	2,030,000	1,210,000
$3,000 — $3,999	470,000	4,810,000	1,830,000	710,000
$4,000 — $5,999	220,000	5,170,000	1,360,000	690,000
$6,000 and over	160,000	3,120,000	630,000	590,000
Total	8,050,000	22,480,000	8,280,000	6,510,000

Source of basic data: U. S. Bureau of the Census, Current Population Reports, Consumer Income, Series P-60, No. 5, February 7, 1949, "Income of Families and Persons in the United States: 1947."

These distinctions are important, as the figures bear out. While incomes are generally higher in urban areas, needs for cash income are less in rural areas where life is simpler, rents and taxes are lower, savings go further in providing a livelihood, and it is easier to have the proverbial garden patch and cow. Such factors, as well as personal preference, swell the rural population of retired persons or couples with small incomes. Thus we see that, of the indicated million and a half families with cash incomes of less than $500, over two-thirds reside in rural communities.

The figures which Senator Flanders wanted explained, the 29.8 per cent and the 4.6 per cent, do not appear in the published Census report. If they were intended to refer to urban families, the percentages seem decidedly too high – even aside from the "reporting biases" referred to earlier. Our table (second column) shows 19.7 per cent under $2,000 and 2.2 per cent under $500.

Our second column shows roughly a half million urban families with incomes under $500 and nearly a million and a half with incomes under $1,000. Doubtless this million and a half includes a fractional part of the public relief case load. During an average month in 1947 State programs participated in by the Federal Government provided relief to 2,276,000 old people, aided in the support of 1,001,000 children in 393,000 families, and helped 79,000 blind persons. Besides charitable programs participated in by the Federal Government, even more people obtained help through local governments without Federal participation; through the tens of thousands of charitable organizations supported by the generosity of the private citizen; and through the benefaction of neighbor to neighbor.

The heaviest burden of public relief and other costs of government is borne by the four million-odd families with incomes of $6,000 and over – the point at which the President wants to raise personal income taxes as a way of financing increased government outlays.

No Measure of a Social Problem

When the question comes up as to how many persons or families have money incomes under stated limits, we too commonly overlook geographical variations in living costs. We overlook the diversities of people and their circumstances, their ages and stages of life, their sources of nonmonetary income, their abilities to cut corners on living expenses, their accumulations of savings, their generosities in helping one another, their strengths and frailties, their unequal ambitions and willingnesses to work to get ahead and to provide for the uncertain future. It is only when such diversities are understood that one can appreciate how, in a year like 1947, when employment opportunities were abundant at good pay, one family in ten could report money income of less than $1,000.

There is no one figure that can be drawn out of an income distribution to measure a magnitude or degree of a social problem. Out of the sheer mechanics of their construction, not to mention biases of reporting, there is bound to be at any time some number of citizens and families below some limits. Such figures, for example, provide no usable measure of needs for home-building. They do not measure the number of families resident in "slum" areas – which everyone would like to see cleaned up. They do not tell who ought to be selected to occupy government apartments, rent-subsidized at the expense of the rest of the population. They do not measure the number of families who are beneficiaries of rent controls. They do not measure the number of families in need of financial relief by charitable organizations or the government, numerous as such needs are in the lowest income brackets.

It is important to recognize, if only because the fact is so frequently neglected, that the figures on incomes below this or that limit also include many people who have been *injured* by Federal government policies. The farm price support program has increased the cost of food. The "cheap money" policy has reduced interest returns on bond holdings and savings accounts. The steeply

progressive income tax has crushed the ability of people with fluctuating incomes to save in good years to take care of themselves in bad years. Even the rent controls, besides helping many families in moderate circumstances, have pressed down into the lowest income bracket others who provided for old-age security by ownership of rental property.

To Senator Flanders' question, who are the people in the lowest money income brackets, there is only one answer of which one can be positive. The group includes all kinds of people – even from millionaires experiencing losses to squatters living off the land. Probably, there are two predominant groupings: those receiving charitable assistance, public or private; and those living on past savings, often supplemented by aid from relatives, some cash income from part-time employment, odd jobs, small pensions, trust funds, dividends, interest, rents and royalties, or non-cash income from a garden and ownership of a home.

The Small Capitalist

There is no indication in the Census figures as to how much public or private relief payments, in cash or in kind, were included in the income figures. But it is doubtful if very many communities today can provide support for a family on less than $500 a year. Often the cost exceeds $1,000 and may exceed $2,000. On this premise, the majority of the families in the very lowest bracket – under $500 – must be living in whole or in part on past savings. This suggests the unexpected conclusion that the "small capitalist" may predominate in the very lowest income bracket. He gets included in all the statistics on incomes below *any* limit. To a large extent, he is today's "forgotten man."

It is a rare family that does not hold some government bonds as well as some direct or indirect investment in the plant and equipment of American business. There are eighty million holders of United States Savings bonds alone. The seventy million policyholders in private life insurance companies provide an absolute minimum of the number of people with stakes in business.

Savings are the prime means by which people are enabled to maintain themselves, in dignity and self-respect, when their earnings decline or cease. Savings at the same time provide essential means to business to create new productive facilities as well as to government to finance deficits which occur in war times and depressions. Taxation which grinds on *ability* to save, combined with welfare benefits that weaken the *incentive* to save, can combine to destroy a free society.

The younger people in the lower brackets comprise the group which has all the opportunities ahead and from which the savings of the future must come. It is the group from which will be drawn future Presidents, leaders in business, the arts and professions, skilled artisans, judges, cabinet members and Congressmen. With the increased responsibilities that are involved in tasks of leadership – and as a stimulus to acceptance of responsibility by the qualified – go financial rewards of above average incomes. Nothing is more corrosive of ambition than excessive taxation of the rewards of effort – with its fellow-traveling doctrine that "the world owes you a living."

No one questions the need for helping people in distress. Aid for the indigent, as old as civilization, can be given on a more generous scale as the nation as a whole becomes richer. The issue becomes a critical one when minimum benefits offered to one and all become interpreted as rights not to work and the load on the productive components of the society is enlarged to a point where the whole nation can suffer from a stagnation of effort to work and of ability and incentive to save. These last principles are not without general recognition, at least "in principle." But no one, in good conscience, should want to probe too far for a breaking point that everyone should know is there.

THE NATIONAL CITY BANK OF NEW YORK

THE NATIONAL CITY BANK OF NEW YORK

***Head Office:* 55 Wall Street, New York**

Condensed Statement of Condition as of March 31, 1949

Including Domestic and Foreign Branches

ASSETS

Cash, Gold and Due from Banks		$1,419,660,246.91
United States Government Obligations (*Direct or Fully Guaranteed*)		1,572,195,071.34
Obligations of Other Federal Agencies		17,988,577.26
State and Municipal Securities		243,833,896.22
Other Securities		88,477,537.97
Loans and Discounts		1,393,086,181.69
Real Estate Loans and Securities		2,430,711.86
Customers' Liability for Acceptances		20,283,245.05
Stock in Federal Reserve Bank		7,500,000.00
Ownership of International Banking Corporation		7,000,000.00
Bank Premises		27,509,105.11
Other Assets		2,634,776.88
Total		$4,802,599,350.29

LIABILITIES

Deposits		$4,444,516,005.89
Liability on Acceptances and Bills	$ 29,178,196.88	
Less: Own Acceptances in Portfolio	7,964,570.18	21,213,626.70
Items in Transit with Branches		13,121,239.06
Reserves for:		
Unearned Discount and Other Unearned Income		5,686,361.15
Interest, Taxes, Other Accrued Expenses, etc.		22,848,328.41
Dividend		2,325,000.00
Capital	$124,000,000.00	
Surplus	126,000,000.00	
Undivided Profits	42,888,789.08	292,888,789.08
Total		$4,802,599,350.29

Figures of Foreign Branches are as of March 25, 1949.

$295,262,995.00 of United States Government Obligations and $568,480.06 of other assets are deposited to secure $210,411,462.87 of Public and Trust Deposits and for other purposes required or permitted by law.

(Member Federal Deposit Insurance Corporation)

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Williamsville, New York

ROBERT WINTHROP
Robert Winthrop & Co.

CITY BANK FARMERS TRUST COMPANY

***Head Office:* 22 William Street, New York**

Condensed Statement of Condition as of March 31, 1949

ASSETS

Cash and Due from Banks		$ 19,133,265.77
United States Government Obligations (*Direct or Fully Guaranteed*)		85,176,429.34
Obligations of Other Federal Agencies		1,044,260.70
State and Municipal Securities		5,364,273.05
Other Securities		100,475.00
Loans and Advances		3,925,004.34
Real Estate Loans and Securities		1,770,695.94
Stock in Federal Reserve Bank		600,000.00
Bank Premises		3,001,272.81
Other Assets		2,504,404.23
Total		$122,620,081.18

LIABILITIES

Deposits		$ 89,677,304.68
Reserves		3,259,824.26
Capital	$10,000,000.00	
Surplus	10,000,000.00	
Undivided Profits	9,682,952.24	29,682,952.24
Total		$122,620,081.18

$7,824,366.88 of United States Government Obligations are deposited to secure $5,994,302.77 of Public Deposits and for other purposes required or permitted by law.

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